Agenda Date: 7/16/03
Agenda Item: 2A

STATE OF NEW JERSEY

Board of Public Utilities
Two Gateway Center
Newark, NJ 07102
www.bpu.state.nj.us

ENERGY

IN THE MATTER OF THE VERIFIED PETITION OF ROCKLAND ELECTRIC COMPANY FOR THE RECOVERY OF ITS DEFERRED BALANCES AND THE ESTABLISHMENT OF NON-DELIVERY RATES EFFECTIVE AUGUST 1, 2003	)	SUMMARY ORDER DOCKET NO. ER02080614
IN THE MATTER OF THE VERIFIED PETITION OF ROCKLAND ELECTRIC COMPANY FOR APPROVAL OF CHANGES IN ELECTRIC RATES, ITS TARIFF FOR ELECTRIC SERVICE, ITS DEPRECIATION RATES, AND FOR OTHER RELIEF	)	DOCKET NO. ER02100724

(SERVICE LIST ATTACHED)

BY THE BOARD:

This Summary Order memorializes, in summary fashion, the action taken by the Board of Public Utilities ("Board") in these matters at its July 16, 2003 public agenda meeting by a vote of five Commissioners. The Summary Order is being issued for the purpose of implementing new rates on August 1, 2003, consistent with the requirements of the Electric Discount and Energy Competition Act ("EDECA"), N.J.S.A. 48:3-49 et. seq. and the Board's Orders implementing EDECA. The Board will issue a more detailed Final Decision and Order in these matters, which will provide a fuller discussion of the issues as well as the reasoning for the Board's determinations.

These matters concern petitions filed by Rockland Electric Company ("RECO," "Company," or "Rockland") requesting (1) recovery of its deferred balances and the establishment of non-delivery rates ("deferred balance case"); and (2) approval of changes in its distribution rates, including changes to its tariff for electric service, its depreciation rates and other relief ("base rate case"). RECO filed its deferred balance case on August 29, 2002 and its base rate case on October 1, 2002. The cases were transmitted to the Office of Administrative Law ("OAL") on September 12, 2002 and October 16, 2002 respectively, and consolidated for hearing.

Additionally, pursuant to the Board's Order dated July 22, 2002*, Order Directing the Filing of Supplemental Testimony and Instituting Proceeding to Consider Audits of Utility Deferrals,* BPU Dkt No. ER02050303, *et al*., an audit was performed on RECO's deferred balances, the results of which were placed in the record of the deferred balance case at the OAL.

These matters come before the Board on a record developed in hearings before Administrative Law Judge ("ALJ") William Gural, who issued an Initial Decision ("I.D.") on June 12, 2003. The parties to the proceeding included the Company, Board Staff and the Ratepayer Advocate ("RPA"). Participant status was granted to Jersey Central Power and Light Company and Public Service Electric and Gas Company. Exceptions and Replies to Exceptions were filed with the Board. After the hearings were completed at the OAL, both the Company and the Ratepayer Advocate supplemented their positions based upon 12 months of actual data.

The Board acknowledges and appreciates the efforts of ALJ Gural in presiding over this consolidated proceeding and in producing a detailed and thorough Initial Decision.

Based on our review of the extensive record in this consolidated proceeding, the Board has determined that the Initial Decision, subject to certain modifications, which will be set forth herein, represents an appropriate resolution of this proceeding. Accordingly, except as specifically noted below, and as will be further explained in a detailed Final Decision and Order which shall be issued, the Board HEREBY ADOPTS and incorporates by reference as if completely set forth herein, as a fair resolution of the issues in this consolidated proceeding, the Initial Decision.

The modifications and clarifications to the Initial Decision which the Board HEREBY ORDERS, are based upon 12 months of actual data and are summarized as follows:

A. Base Rate Case

1. The ALJ concurred with RECO's position that a 12% return on equity with an overall rate of return of 9.33% is appropriate. The Ratepayer Advocate ("RPA") recommended a return on equity of 9.25% and an overall rate of return of 7.92%. Staff recommended a return on equity of 9.5% and an overall rate of return of 7.90%. For reasons that will be further explained in a detailed Final Order which shall be issued, the Board HEREBY FINDS that, based on the evidence in the record and in light of current market conditions, the capital structure and level of return recommended by the ALJ are unreasonable. Accordingly, the Board HEREBY MODIFIES the ALJ's Decision with respect to capital structure and return on equity and HEREBY ORDERS (1) that RECO's appropriate return on equity is 9.75%, with an overall rate of return of 8.02%; and (2) that the capital structure and embedded cost of debt to be employed for ratemaking purposes is as follows:

TYPE OF CAPITAL	RATIOS	RATE	WEIGHTED COST RATE
LONG-TERM DEBT	54.00%	6.54%	3.53%
EQUITY	46.00%	9.75%	4.49%
TOTAL CAPITAL	100.00%		8.02%

2. The Board HEREBY REJECTS the ALJ's Initial Decision that no adjustment should be made to reflect consolidated tax savings and HEREBY ADOPTS the position taken by Staff in its Reply Brief that rate base should be reduced by $1.329 million to reflect tax savings achieved by RECO through offsetting tax losses of affiliates with RECO's positive taxable income. The Board concurs with Staff that, consistent with longstanding Board policy, these savings should be shared with customers.

3. All the parties in the base rate case agree that there is a significant excess depreciation reserve. The Company proposed a 20-year amortization of its calculated reserve excess of $11.8 million. The RPA claimed the proper reserve excess was $22.1 million, based upon the Company's asset lives, but excluding the Company's future net salvage assumptions from the depreciation rates. The RPA accepted the Company's proposal of a 20-year amortization. Both Staff and the ALJ adopted the RPA's recommendation. The Board HEREBY MODIFIES the Initial Decision so that the RPA's recommended level of excess reserve is amortized back to ratepayers over 10 years. The Board finds this to be an appropriate action in order to offset the increase associated with the deferred balances that were incurred over the 4-year transition period, as well as the increase in BGS charges for current service.

4. The ALJ did not specifically address certain issues but instead implicitly adopted Staff's position on these issues by adopting Staff's pro-forma operating income. Accordingly the Board HEREBY ADOPTS Staff's recommendations with regard to these issues, which include miscellaneous service revenues, electric rent revenues and removal of certain incentive compensation expenses.

5. While the Board ADOPTS the Initial Decision concerning Pension Expense and Other Post- Employment Benefits ("OPEBs"), the Board FURTHER DIRECTS RECO to cease its deferred accounting treatment for pension expense and OPEBs relative to the difference between the amounts allowed in rates and the book expense. The Board notes that RECO was the only utility that was allowed to use this type of deferred accounting for such expenses and that on a going forward basis, in order to provide consistency among the utilities, this deferred accounting treatment is no longer appropriate.

6. The Board HEREBY ADOPTS Staff's recommendation to include the Company's proposed 12-month actual adjustment of $0.225 million to expenses related to the Company's common expense allocation, as this amount reflects the elimination of the double-count issue raised on the record. In addition, the Board HEREBY ADOPTS Staff's recommendation to include the Company's proposed 12-month actual adjustment of $0.031 million for maintenance costs of additional telephone lines installed due to the implementation of the hourly energy pricing program. It is also noted that other investment associated with the hourly energy pricing program has been reflected in this case without opposition by any party.

7. The Board HEREBY ADOPTS the recommendation by Staff and the RPA to reflect only that portion of interest expense on customer deposits associated with the customer deposit balance deducted from rate base.

8. With regard to Utility Plant In Service, the Board HEREBY MODIFIES the ALJ's Initial Decision and authorizes the Company to file a Phase II proceeding on or before

September 1, 2004 to address the Upper Saddle River and the Darlington projects and associated flow-through impacts that the record reflects and the ALJ properly found were not completed in the test year. The Board HEREBY ORDERS that the Company be permitted to include in this Phase II filing a request for recovery of the costs of reliability enhancements, which it had sought in this case, but the record reflected and the ALJ appropriately concluded, had not actually been performed. As part of the Phase 2 proceeding, the Board FURTHER ORDERS that the parties review whether these or other projects included in the proceeding are transmission related or are distribution related. RECO will have the burden of proof with respect to the classification of these facilities as transmission (FERC-regulated) or distribution (BPU-regulated) plant.

9. The Board HEREBY REJECTS the ALJ's finding in the Initial Decision that no change be made in the bad check charge and the reconnection charge. In recognition of the record presented concerning the actual costs associated with these charges, the Board HEREBY ORDERS that the bad check charge be raised from $3.50 to a flat fee of $7.00 and that the reconnection charge be raised from $7.00 to $21.00 for all time periods. Additionally, the Board HEREBY ADOPTS RECO's proposal on line extension charges for new residential subdivisions and multiple occupancy buildings, which updates the charges to reflect current costs, as well as its proposed late payment fee for non-residential and non-governmental customers.

10. In summary, the modifications summarized herein result in a decrease in distribution rates of $7.217 million, which equates to an overall percentage base rate decrease of 5.3%.

B. Deferred Balance Case

1. Although the Board recognizes the valuable analysis performed by the Board's Auditors, Synapse Energy Economics, Inc. ("Synapse") (deferred balances) and Larkin & Associates, PLLC (accounting issues), including Synapse's analysis and recommendation to disallow $26.8 million (excluding interest) from RECO's Basic Generation Service ("BGS") deferred balance related to an asserted possible extension in the parent company's Transition Power Sales Agreements ("TPSA") with the purchaser of its divested generating assets, and related avoidance of hedging costs, in view of the totality of the record, the Board HEREBY ADOPTS the $14.0 million in TPSA and hedging cost disallowances recommended by Staff in its Initial Brief and accepted by the ALJ, and HEREBY reduces the BGS deferred balance by this amount.

2. The ALJ agreed with the opinion of Synapse regarding the timeliness of RECO's transfer of its Eastern Division, which serves approximately 90% of its load, from the New York Independent System Operator ("NYISO") to the Pennsylvania-New Jersey-Maryland Interconnection, L.L.C. ("PJM"). In so doing, the ALJ rejected the position of the RPA that the transfer to PJM should have occurred as early as August 1, 1999. The majority of the Board agrees with the Staff position set forth in its Initial Brief that RECO should have taken the necessary preliminary steps to initiate the transfer four months sooner than it did, and should not have required two months following the FERC's approval to install the necessary metering and communication equipment. Therefore, the Board HEREBY MODIFIES the Initial Decision so as to disallow an additional $2.2 million of the

BGS deferred balance recommended by Staff as an appropriate PJM transfer delay adjustment.

It must be noted that the Board's determination on this issue was by a vote of 3 to 2, with Commissioners Murphy and Alter dissenting. Although concurring with the overall disallowance amount for RECO's BGS deferral, Commissioners Murphy and Alter were opposed to finding the Company responsible for the PJM transfer delay. The positions of the Commissioners will be further amplified and included in the Final Decision and Order.

3. The ALJ recognized $0.3 million of labor and overhead costs associated with RECO's participation in the statewide auction for year 4 of the transition period, and with RECO's implementation of the PJM transfer, as appropriately includable in RECO's deferred BGS balance. The Board agrees with Staff and the RPA that the record does not support a presumption that these costs represent incremental expenses not already recovered through base rates. Accordingly, the Board HEREBY MODIFIES the Initial Decision and disallows the $0.3 million from RECO's BGS deferred balance.

4. The deferred BGS balance on which the Initial Decision was based reflected actual data through November 30, 2002 ($91.2 million of energy costs[1] and accrued interest of $9.3 million, for a total deferred BGS balance of $100.5 million). By letter dated July 3, 2003, the Company updated its deferred balances to reflect an additional six months of actual data (December 2002 through May 2003), and, pursuant to the Board's Order *I/M/O the Establishment of a Universal Service Fund Pursuant to Section 12, of the Electric Discount and Energy Competition Act of 1999*, BPU Dkt. No. EX00020091, to include $1.0 million of Universal Service Fund ("USF") costs in its Societal Benefits Charge ("SBC"). After updating to reflect the additional actual data, the Company's deferred BGS balance is currently projected to be $102.0 million ($92.6 million of energy costs and $9.4 million of accrued interest) as of July 31, 2003, the end of the transition period. After reflecting the ALJ's recommended TPSA and hedging cost disallowances of $14.0 million, Staff's recommended $2.2 million PJM delay disallowance, the RPA and Staff's recommended disallowance of $0.3 million of PJM transfer and BGS auction costs and $1.9 million of disallowed accrued interest, and subject to a true-up to reflect: 1) additional actual data through July 31, 2003; 2) the results of the Board's Phase II Audit of the Company's deferred BGS balance; and 3) a re-calculation of accrued interest to reflect all such disallowances and adjustments, the Board HEREBY AUTHORIZES the recovery of a deferred BGS balance of $83.6 million. The Board additionally HEREBY APPROVES, pending the Board's decision on the Company's securitization petition filed on November 8, 2002, interim BGS deferral recovery of $8.718 million per year before application of the 6% New Jersey Sales and Use Tax ("SUT"). As recommended by Staff,[2] this recovery is based on a 10-year amortization of the recoverable BGS balance "net of tax" (i.e., after deducting accumulated deferred income taxes associated with the deferred costs from the balance) and an interest rate equal to the yield on one-year

[1] The cost of energy and capacity purchased from the NYISO and PJM, and under the TPSAs and power purchase agreements with non-utility generators ("NUGs") priced at market, as well as hedging and Eastern load pocket costs and PJM transfer and BGS auction administrative costs.

[2] Pursuant to a letter from the Board's Secretary dated March 25, 2003, the issue of interim deferral recovery was not addressed by the ALJ.

constant-maturity Treasury notes plus 30 basis points, which is determined herein to be 1.3%.[3]

5. In reference to the ALJ's findings with respect to the other components of the Company's unbundled rates, its Energy Cost Adjustment ("ECA") for the recovery of above-market NUG costs, the SBC and a temporary credit implemented as part of the year-four rate reduction mandated by the EDECA, the Board HEREBY REJECTS the ALJ's finding that a portion of the ECA overrecovery ($3.7 million) be used to offset the BGS deferred balance, and FINDS instead that it be reserved to offset anticipated future underrecoveries of NUG costs, as proposed by the Company. The Board also HEREBY APPROVES the Company's proposed treatment of the remaining ECA overrecovery, the expiration of the temporary credit, and the Company's SBC charges, including the inclusion of $1.0 million of USF costs, as discussed above.

6. While the Company has agreed that interest during the transition period should be accrued net of tax (that accumulated deferred income taxes associated with the deferred costs be deducted from the deferred balance on which interest is accrued), the Board HEREBY DIRECTS the Company to calculate its interim deferral recovery on the same net of tax basis, as set forth above. Additionally, going forward, the interest rate on the Company's short-term debt (debt maturing in less than one year) [4] shall be used as the interest rate applicable to the Company's post August 1, 2003 BGS, ECA and SBC deferrals, and the interest shall also be calculated net of tax.

In addition to reflecting the ordered base rate reduction of 5.3% as discussed in section A, supra, as well as the interim recovery of the BGS deferred balance, the revised SBC, the unchanged ECA, and the expiration of the temporary credit implemented as part of the year-four rate reduction mandated by the EDECA, as discussed in Section B, supra, an additional adjustment to RECO's rates must be reflected herein, effective August 1, 2003, to recover an estimated increase in BGS charges commencing August 1, 2003, resulting from the auction results previously approved by Board Order dated February 6, 2003, BPU Dkt. No. EX0111075.

The net result of these adjustments is an overall increase in the Company's annual retail revenues of approximately $21.125 million for the Fixed Price customers. The Board HEREBY APPROVES this overall increase for service rendered on and after August 1, 2003. Additionally, the Board HEREBY ADOPTS the recommendations of Staff and RECO that the rate increase be implemented on an across-the-board basis, except for a noncontested reduction in the differential in the winter tail block rate for Service Classification No. 5. For the average residential customer (SC-1) using 880 kwh per month on an annual basis this translates into an increase in rates, including an estimated 11.3% increase in BGS charges, amounting to approximately 15.4% (from $85.21 per month to $98.36 per month).

Within five (5) days of the date of this Order, the Company is HEREBY DIRECTED to submit to the Board final revised tariff pages conforming to the terms and conditions of this Summary Order. The Company shall consult with Staff to assure the adequacy of the required submissions.

---

[3] Based upon the rate for the week ending June 27, 2003, as reported in the Federal Reserve Statistical Release dated July 1, 2003.

[4] Or the rate on equivalent temporary cash investments if the Company has no short-term debt outstanding.

Finally, consistent with the recommendation of Staff, the Board HEREBY DIRECTS the Company to file monthly reports with the Board that show, for its share of each NUG project, the energy and capacity purchased (MWH and MW) the amount paid for the energy and capacity, the disposition of the energy and capacity, (i.e. whether it was sold in the wholesale power market or otherwise), the amount received from the sale of the energy and capacity, as well as the value of the energy if it were priced at the average monthly PJM and NYISO LMPs and capacity deficiency rates, and the value if it were priced at the rate payable for BGS supply obtained pursuant to the statewide auction.

DATED: July 31, 2003

BOARD OF PUBLIC UTILITIES
BY:

SIGNED

JEANNE M. FOX
PRESIDENT

SIGNED

FREDERICK F. BUTLER
COMMISSIONER

SIGNED

CAROL J. MURPHY
COMMISSIONER

SIGNED

CONNIE O. HUGHES
COMMISSIONER

SIGNED

JACK ALTER
COMMISSIONER

ATTEST:

SIGNED

KRISTI IZZO
SECRETARY